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UNCLAS SECTION 01 OF 02 LILONGWE 000896

SIPDIS

SENSITIVE

STATE FOR AF/S ADRIENNE GALANEK
STATE FOR EB/IFD/ODF MARLENE BREEN
STATE FOR EB/IFD/OMA FRANCES CHISHOLM
TREASURY FOR INTERNATIONAL AFFAIRS/AFRICA LUKAS KOHLER

E.O. 12958: N/A

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SUBJECT: MALAWI HAS THE MONEY--NOW WHAT?

REF: LILONGWE 854

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SUMMARY

1. (U) The World Bank vice president for Africa recently briefed donors in Lilongwe, confirming that the Bank was disbursing \$25 million in order to support the new government's fiscal reform agenda and to avoid a currency crisis. He reported that the GOM is looking to raise the bar on economic performance and that the Bank is emphasizing the need to improve the investment climate. Both the Bank and donors continue to express cautious support for Mutharika's fiscal agenda, stressing that it depends on continued performance.

WORLD BANK TO MALAWI: KEEP GOING

2. (SBU) At a briefing for donor chiefs of mission in Lilongwe on September 13, World Bank vice president for Africa Callisto Madavo gave his perspective on a round of meetings with GOM officials centered on the disbursement of the first half of a \$50 million structural adjustment credit. He confirmed that the Bank took early action for two reasons: to give an encouraging signal to the reformist government of President Bingu wa Mutharika, and to provide balance of payment support before seasonal foreign exchange pressure produces a currency crisis (see reftel). After acknowledging Mutharika's progress in imposing fiscal discipline and prosecuting corruption, Madavo made it clear that the Bank will release the second tranche only if its established triggers are hit.

3. (U) Madavo portrayed the Bank as being concerned in the medium term about accelerating growth from the current 4 percent to 6, the level targeted for long-term poverty reduction. The Bank sees two main priorities: increase in agricultural productivity (suffering from years of malpractice and neglect) and creation of a confidence-inspiring climate for new investment. Madavo stressed that enabling private-sector growth is the only alternative to continued dependence and poverty. The Bank hopes to reorient thinking about the economy from poverty reduction to wealth creation.

4. (U) According to Madavo, in his meetings with Minister of Finance Goodall Gondwe he heard an interest in "raising the level of ambition," to get beyond the current crisis and make Malawi a performer in the region. Gondwe has said the country should be well positioned to do this without dramatic funding increases, because program implementation has plenty of room for improvement. Gondwe is reported to have asked Madavo to carry a message to donors to allow him "space to operate"--meaning some latitude and time to consider different policy options and directions.

DONORS: CAN OPTIMISM BE REALISTIC?

5. (SBU) The donor reaction to Madavo's presentation was positive, but several representatives took pains to register continued concern about budgetary discipline. One donor expressed particular concern about promised fertilizer subsidies; accounts of the subsidy program have ranged from a highly targeted subsidy to a general price reduction subsidy. (NOTE: In a subsequent conversation, Gondwe said opposition MPs are pressing for a general subsidy; he reported that he is demanding a zero-sum approach to the budget, and that MPs are reluctant to propose realistic trade-offs. The public confusion about what subsidy is actually in the budget can be

explained by the fact that the political battle is still in progress. End Note.) Other donors noted that the signals from the Mutharika government are not perfectly clear, and that there is plenty of precedent for fiscal recidivism. These expressions of skepticism notwithstanding, the donors are following the Bank's lead in opening their purses: Norway is considering release of a \$3 million tranche of budget support, and the UK intends to release nearly \$9 million during Mutharika's September visit to London, with another \$18 million by the end of the calendar year.

COMMENT: STAYING SOBER AIN'T EASY

16. (SBU) Madavo's message, as represented to the donors, is dead right. We were encouraged to hear the practical reasoning for the September disbursement, and agree that any congratulations must be accompanied by the reminder that we are still watching. One benefit of an early Bank disbursal is that it allows everyone to see how this government behaves when it is relatively flush, especially given the presence of an IMF staff monitoring program. The more seasoned members of the donor community here are the most skeptical, having heard more or less the same promises many times before. However strong the public support for responsible governance, there is constant political pressure to return to old spending habits, based on widespread ignorance of--or disregard for--clear economic imperatives. (Though considering the donors' forgiving behavior in the past, the reality of economic imperatives here may not be so clear.)

17. (SBU) Gondwe's recent budget address to Parliament stressed the need for a series of transitional budgets to put the house back in order, followed by more ambitious developmental budgets once investment money becomes available. One hopes that Parliament will have enough patience, and the administration enough discipline, to avoid the lapse that so many here seem to expect. This much is certain: sound but dull fiscal policy does not have the popular appeal of reckless handouts, and seeing it through will involve real political risk. It is up to the donors to make it clear that breaking discipline will carry its own risks.

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